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TREASURY FOR OFFICE OF SOUTH ASIA MKAPLAN
USDA PASS FAS/OCRA/RADLER/BEAN/FERUS

E.O. 12958: N/A
TAGS: ETRD ECON EFIN IN
SUBJECT: GOI ANNOUNCES ADDITIONAL ASSISTANCE FOR EXPORTERS

¶1. Summary: In a bid to boost the Indian export sector, Minister of Commerce and Industry Anand Sharma on January 12 announced new sector-specific export incentives that retroactively took effect on January 1. The benefits include expansion of products and destinations eligible for various export promotion schemes and inclusion of specific products entitled for duty neutralization schemes. These benefits are in addition to the ones that had been announced in India's five-year Foreign Trade Policy in August 2009. The Commerce Ministry will fund the cost of the new measures, estimated at around five billion rupees (approximately $105 million), from its budgetary resources. While the Finance Ministry has been concerned about export incentives contributing to the swelling fiscal deficit, the Commerce Ministry and export industry groups have been demanding government support to stimulate India's export performance, which faced continual monthly declines between October 2008 and October 2009. The Commerce Ministry has also proposed reduced interest rates on dollar credit to improve export profits and continuation of discounted interest rates for labor-intensive sectors (introduced as part of last year's stimulus spending) -- measures that the Finance Ministry will need to approve. Despite the recent recovery in overall exports, which is partially attributable to the base effect, Minister Sharma believes certain sectors still need additional government support. End summary.

Debate on Export Stimulus Package

¶2. With the backdrop of a hot debate in government circles over the continuation of a stimulus package for exports, Commerce Minister Sharma, on January 12, announced new measures to give a boost to India's export sector. The Finance Ministry has opposed the continuation of the stimulus packages to industry in view of loss of revenues on account of duty rebates and the increasing fiscal deficit (projected to be 6.8 percent of GDP in FY 2009-10). Finance Secretary Ashok Chawla had reportedly said that continuing stimulus measures was not good for the economy, arguing that "too much of stimulus can be injurious to health." His views have come in sharp contrast to those of Minister Sharma, who indicated that his ministry has reviewed various export sectors, and some are still facing problems despite overall positive export growth since November 2009. The sectors need government support until they return to strong growth patterns, especially in view of the continuing depressed demand in major western markets.

Commerce Will Cover Cost

¶3. Sharma made clear that the Commerce Ministry will bear the cost of the new benefits, estimated at around five billion rupees

(approximately $105 million), using its annual budget allocation. The new measures include addition of 237 items to the list of products entitled for credits (of two-five percent of the free-on-board value of the export) under the Focus Product Scheme (FPS), which is meant to promote export of products which have high employment intensity in rural and semi-rural areas and offset infrastructure inefficiencies and higher marketing costs. The new products include items in the engineering, electronics, rubber, chemicals, and plastic sectors. The Commerce Ministry also added 1837 new products (e.g., machine tools, earth moving equipments, transmission towers, electrical equipments, steel tubes and pipes, compressors, and auto components) to the Market-Linked FPS. It added China and Japan to the list of export destinations that are eligible for duty credits, as part of India's efforts to diversify away from exports to the United States and Europe. In addition, the Commerce Ministry has submitted a request to the Finance Ministry to approve continuation of interest discounts for exporters and allow reduced interest rates for dollar credit in view of the strengthening rupee. Minister Sharma told a group of exporters on January 23 that this request included continuation of subsidized two-percent interest rate credit for labor intensive sectors such as textiles, handicrafts, carpets, leather, gems and jewelry. While the new export promotion schemes are made retroactive to January 1, 2010, the interest subsidy proposals will need to be approved by the Finance Ministry as part of the upcoming budget.

India's Exports on Recovery Path

¶4. Stimulus packages consisting of tax cuts, increased government expenditure, easy credit and interest rate cuts were announced in

three phases between September 2008 and April 2009, which, according to many trade observers and government officials, have helped India's export sector recover. According to the latest data announced by Minister Sharma at a recent conference in Mumbai, exports have grown 9.4 percent to $14.6 billion in December 2009 over the previous month (which would be a 15 percent increase over December 2008), with strong growth in the pharmaceutical, engineering and auto components sectors. Exports in November 2009 registered positive year-on-year growth (18 percent) for the first time since they began plunging with the onset of global recession in October 2008. India's cumulative exports for the eight-month period from April to November 2009 were still down 22.3 percent from the same period the previous year. The Commerce Minister expects to maintain momentum in exports but he has emphasized ongoing concern regarding the sluggish demand in India's major export markets.

Comment

¶5. Minister Sharma is right to view the recent positive export growth figures with caution, especially considering that they are now rising from a very low base. But the fiscal deficit must be managed, too. The GOI is scheduled to present its annual budget on February 26 before which the Finance Ministry must make a decision about the proposed subsidized interest rates for exporters. In addition to the compelling need to manage its unsustainable fiscal deficit, the GOI has ahead a daunting task of dealing with very high food inflation. Post is monitoring future GOI steps in this direction and will report accordingly.

Roemer